ONLINE LENDER TUG-OF-WAR

Winning with exceptional customer experience without falling prey to fraud
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The online lending industry continues to grow at a rapid pace and is now serving a broader customer base, providing more diversified loan types, and leveraging technology and data to approve or decline applicants in record time. Technological innovation and attractive investment opportunities have fueled the industry’s rapid growth, increasing the size of the addressable market and providing a wide array of consumers with fast and easy access to capital. With a market size expected to reach $350 billion by 2025, online lenders must balance the elevated expectations of today’s consumers with the need to be profitable, increased competition, and consistently rising fraud rates.

Rising consumer expectations have introduced a “need for speed,” and further amplified the importance of approving applicants quickly. Meanwhile, the floodgates have opened for unqualified and fraudulent applicants to seep into underwriting - introducing all new levels of risk to the industry. Based on a recent study from LexisNexis, digital lending has one of the highest fraud rates of any industry, with a staggering 36% of lending applicants suspected to be fraudulent.

For online lenders to stay competitive, maintain quality loan standards, and keep profits high, they must adopt smarter practices and have access to quality data and intelligent decision engines to find and serve their best customers. As the industry advances, third party resources are more readily available to help achieve these goals. Their challenge is to deliver a simplified customer experience, implement advanced applicant filtering, and create near instant “decisioning” in an effort to avoid first payment defaults and ultimately lower the cost per fund.

Simplifying the customer experience can easily be achieved through third-party sources such as marketing firms, data providers, and platforms. According to a recent Ernst and Young report, “Alternative lenders have effectively served various untapped markets, and have done this by creating business models where they outsource non-core functions and focus on excelling at those capabilities that will create a strong value proposition and bring the best possible user experience to their customers.”

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1 https://www.researchandmarkets.com/research/qhjr6v/us_alternative
2 http://frankonfraud.com/fraud-reporting/new-study-shows-lenders-have-the-highest-cost-of-fraud/
Competitive interest rates have historically been perceived as the main driver in winning a consumer’s business. While interest rates remain important, recent studies show the overall customer experience is just as, if not more, important. According to a PwC survey, consumer expectations have shifted, with speed, transparency, and customer service now making up more than 50% of the decision making criteria. This new trend uncovers opportunities for lenders to capture market share by facilitating a simplified customer experience as a competitive advantage.

Keys to a successful, simplified customer experience

1. Identify a target market and create a strategy
2. Facilitate a personalized online experience
3. Deliver an expedited application process
4. Use a layered approach to filter applications

It’s important to identify and profile a target market and then create an outreach strategy specific to that audience in order to win the right customers. Depending on your goals, strategies for reaching a target market will vary, from inbound marketing campaigns, to channel partnerships. Once the target market is reached, facilitating a personalized online experience is crucial to winning customers. As a rule of thumb, consumers should be able to understand the types of loans offered, the value proposition of the lender, and how to take action within 7 seconds.

Personalization for the user can take shape in many ways – for example, providing localization options to cater to the needs of your target market.

Once a consumer decides to take action, the application process needs to be quick and simple. Drop-off rates will always increase as customer friction occurs, driving good applicants to competitive sites that offer a more streamlined experience. In order to reduce customer friction, advanced filtering practices, such as cross-verifying identity information and using third-party data providers, can help speed up this process.

Oportun, an online and physical lender based out of Northern California, asks immediately upon accessing their website what language the user prefers to create a better user experience for the target demographics.

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2. [https://www.tributemedia.com/blog/you-have-7-seconds-what-a-visitor-should-know-about-your-website-within-moments](https://www.tributemedia.com/blog/you-have-7-seconds-what-a-visitor-should-know-about-your-website-within-moments)
Filtered Approach to Screening

A simplified consumer experience during the application process makes it easier for good customers to apply, but also makes it easier for fraudsters to do so at scale. The screening phase is a waiting game for the applicant that the fastest lender usually wins. As lengthy application and approval processes are being scaled back to meet the needs of good customers, it makes it more difficult to easily weed out bad applicants.

As online lenders continue to receive a broader range of applicants, such as subprime, thin-file, and underserved markets, optimizing the screening process requires layering the right tools. For online lenders to mitigate fraud and speed good applicants through the funnel, they need to leverage machine learning capabilities using positive and negative risk signals, traditional and non-traditional (digital) data signals, and linkages between these attributes to get a clearer picture of the identity. These tools must perform with speed and accuracy to combat synthetic identity theft and detect new fraud trends as they emerge. With quick access to internal databases and low-latency 3rd party API calls at the top of the funnel, applications can be screened more quickly through the necessary filters, and in priority order based on respective cost.

Filtering for speed and cost

First: Internal data and free filters (instantaneous)

This is where the cheapest and quickest filters should live. Of all the other filters, these will have near-zero latency and no external cost to the lender. Examples include internal blacklists, duplicate applications, and velocity checks.

Second: Quality filters (~1s)

Quality filters can provide actionable insights using both positive and negative identity data signals early in the screening process at costs as low as a cent - to fractions of a cent per query. Examples include device ID, user behavior, identity data, network data, and linkages between identity data attributes.
POSITIVE DATA SIGNALS INCLUDE

- Email-to-name match
- Address-to-name match
- IP-to-address proximity
- Low risk scores
- Phone-to-name match
- Phone-to-address match
- Email in use >720 days

NEGATIVE DATA SIGNALS INCLUDE

- Email address is less than 90 days old
- Non-fixed VoIP or toll-free communication lines
- Phone country code doesn’t match address
- Proxy IP address is used
- Email, phone, or address doesn’t match name
- Carriers with higher levels of fraudulent accounts
- Phone, email, or address is invalid
- IP more than 100 miles from address or phone

Data points and signals gained from quality filters mean different things for different lenders, depending on the areas in which the lender operates. For example, purchasing leads is a major cost center for lenders, especially when only a small percentage of those leads actually convert into loans with the portfolio operator. A leading loan origination company believed the efficiency of their automated purchasing process could be improved with fraud mitigation and application screening earlier in the process. Using data analysis and machine learning, they examined key trends of fraudulent leads and were able to see patterns from specific phone carriers. The company implemented Ekata Identity Check API to identify key indicators that allowed them to automatically eliminate bad leads and more than double conversion rates.5

Case Study:
Loan Origination Company Doubles Conversions While Slashing Costs

10% of bad leads were eliminated by identifying four key indicators that a purchased lead was not likely to convert, including three wireless carriers and a proxy IP address.

Weeding out leads with these four indicators helped reduce the cost per funding from $109 to $92—a savings of 15% even after accounting for the additional cost of Ekata.

Conversion rates improved across the companies entire portfolio. In one case the company went from purchasing an average of 163 leads to 113 leads a day, while the conversion rate more than doubled from 15% to 30.22%.

5 http://procampaigns.whitepages.com/rs/756-OJA-475/images/CaseStudy_Success_Loan_Organization.pdf
Third: Mandatory filters (minutes)

Mandatory filters are the most costly and include checks such as AML and KYC compliance, income verification, and credit pulls from both traditional and alternative credit bureaus. The cost of processing these checks alone is high, with the risk of default even higher. A 2017 LexisNexis study reported digital lenders incur costs of $3.07 for every dollar of fraud — over 3x the cost of the actual loss itself. These costs can be reduced by weeding out fraudulent applicants prior to the underwriting process and paying for mandatory filters.

This layered filtering approach results in a lower cost per fund by identifying fraud earlier and creating multiple underwriting pathways behind the scenes. For the borrower, the end result is a decision in minutes. For the lender — a herculean effort to identify, classify, and decision at break-neck speeds. Implementing layered filtering requires online lenders to identify an appropriate platform strategy for their lending operation.

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6 http://frankonfraud.com/fraud-reporting/new-study-shows-lenders-have-the-highest-cost-of-fraud/
Optimized Decisioning Process

Alternative lenders now leverage as many as 50 data points when processing a consumer application in order to assess risk, reduce fraud, and continue to push good customers through the process. Therefore, the question is no longer whether the data is needed, the questions they’re now asking are:

1. How do I find the most valuable data sources, AND
2. How do I ingest them as quickly as possible

This is where quality data unites with proprietary, hybrid, and/or third-party platforms, and machine learning to automate the verification and decisioning process.

On one end of the spectrum, lenders such as Upstart invest heavily in proprietary technology and data science, and recently reported instant approval rates of more than one third of loans. “At some point, we think 80 to 90 percent of loans will be completely automated,” Upstart’s CEO said. Companies like Upstart are leveraging quality data, networks, and machine learning models to adapt as loan payments and defaults happen.

Lenders without these in-house resources can remain competitive by outsourcing to vendors that provide the same services. Third-party resources support these strategies by providing lenders with access to:

- Quality data and sophisticated data science
- Secure infrastructures and pipelines to ingest broader data sets
- Machine learning know-how, models, and scores

These resources improve their ability to identify, qualify, and confidently decide within a streamlined process, resulting in higher profits and fewer defaults.

“Alternative lenders remain nimble and cost efficient by leveraging analytics and open architecture to integrate with 3rd parties.”

E&Y: Alternative Lenders

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Conclusion

With the ever-increasing demand for top-notch online customer experiences, it’s as important to identify good applicants, as it is to focus on weeding out fraud. Customers are looking for fast and simple ways to access alternative funds for a multitude of reasons, with their needs and wants in the hands of online lenders. It’s not enough to just have a convenient, easy-to-use loan application process; the expectation is for instant approvals and fast funding of their loans. That means it’s not about “nice to haves” for online lenders, but the must have of a full arsenal — quality data, technology and tools, infrastructure, and the right layered filtering process that expedites consumer onboarding and approvals, while safeguarding against fraud.

SUCCESS STORY

Online Lender Increases Efficiency And Qualifies More Good Loans

Learn more

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4 Gartner, Align Your Financial Fraud Detection Strategy With Gartner’s Capability Model, Published: 26 July 2017 ID: G00325850
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